ALANCO TECHNOLOGIES INC
Form 10-Q
May 16, 2011

ALANCO TECHNOLOGIES, INC.

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

_ X QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2011

____TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT
For the transition period from _____________ to ____________

Commission file number 0-9347

ALANCO TECHNOLOGIES, INC.
(Exact name of registrant as specified in its charter)

Arizona
(State or other jurisdiction of incorporation or organization)

86-0220694
(I.R.S. Employer Identification No.)

15575 N. 83rd Way, Suite 3, Scottsdale, Arizona 85260
(Address of principal executive offices) (Zip Code)

(480) 607-1010
(Registrant's telephone number)

____
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements in the past 90 days. X Yes ___ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	___	Accelerated filer	___
Non-accelerated file	___	Smaller reporting company	X

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act)
___ Yes X No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:
As of May 4, 2011 there were 5,567,700 shares of common stock outstanding.

1

ALANCO TECHNOLOGIES, INC.

INDEX

ALANCO TECHNOLOGIES, INC.

Forward-Looking Statements: Except for historical information, the statements contained herein are forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include statements concerning plans, objectives, goals, strategies, future events or performance, and underlying assumptions and other statements, which are other than statements of historical facts. The words “believe,” “may,” “estimate,” “continue,” “anticipate,” “intend,” ”should,” “plan,” “could,” “target,” “pote “will,” “expect” and similar expressions, as they relate to the Company are intended to identify forward-looking statements within the meaning of the “safe harbor” provisions of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended. From time to time, the Company may publish or otherwise make available forward-looking statements of this nature. All such forward-looking statements are based on the expectations of management when made and are subject to, and are qualified by, risks and uncertainties that could cause actual results to differ materially from those expressed or implied by those statements. These risks and uncertainties include, but are not limited to, the following factors, among others, that could affect the outcome of the Company's forward-looking statements: general economic and market conditions; reduced demand for information technology equipment; competitive pricing and difficulty managing product costs; development of new technologies which make the Company's products obsolete; rapid industry changes; failure by the Company's suppliers to meet quality or delivery requirements; the inability to attract, hire and retain key personnel; failure of an acquired business to further the Company's strategies; the difficulty of integrating an acquired business; undetected problems in the Company's products; the failure of the Company's intellectual property to be adequately protected; unforeseen litigation; unfavorable result of current pending litigation; the ability to maintain sufficient liquidity in order to support operations; the ability to maintain satisfactory relationships with lenders and to remain in compliance with financial loan covenants and other requirements under current banking agreements; the ability to maintain satisfactory relationships with suppliers; federal and/or state regulatory and legislative actions; customer preferences and spending patterns; the ability to implement or adjust to new technologies and the ability to secure and maintain key contracts and relationships. New risk factors emerge from time to time and it is not possible to accurately predict all such risk factors, nor can we assess the impact of all such risk factors on our business or the extent to which any risk factor, or combination of risk factors, may cause results to differ materially from those contained in any forward-looking statements. Except as otherwise required by applicable law, we undertake no obligation to publicly update or revise any forward-looking statements or the risk factors described in this Quarterly Report or in the documents we incorporate by reference, whether as a result of new information, future events, changed circumstances or any other reason after the date of this Quarterly Report on Form 10-Q.

ALANCO TECHNOLOGIES, INC.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

CONDENSED CONSOLIDATED BALANCE SHEETS
AS OF MARCH 31, 2011 AND JUNE 30, 2010

	March 31, 2011 (unaudited)	June 30, 2010
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 183,600	$ 152,100
Assets held for sale	17,873,000	20,243,200
Prepaid expenses and other current assets	221,800	100,000
Total current assets	18,278,400	20,495,300
PROPERTY AND EQUIPMENT, NET	400	900
TOTAL ASSETS	$ 18,278,800	$ 20,496,200
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable and accrued expenses	$ 602,100	$ 581,700
Dividends payable	50,400	56,400
Notes payable, current	4,757,900	6,328,000
Liabilites related to assets held for sale	3,926,000	3,545,900
TOTAL LIABILITIES	9,336,400	10,512,000
Preferred Stock - Series B Convertible - 500,000 shares authorized, 119,700 and 111,200 issued and outstanding, respectively	1,183,600	1,098,500
SHAREHOLDERS' EQUITY		
Preferred Stock - Series D Convertible - 500,000 shares authorized, 82,300 and 134,200 shares issued and outstanding, respectively	814,900	1,333,800
Preferred Stock - Series E Convertible - 750,000 shares		

authorized, 725,000 and 735,000 shares issued and outstanding, respectively	3,165,900	3,210,900
Common Stock - 75,000,000 authorized, 5,534,500 and 4,665,500 shares outstanding, net of 2,000 shares of Treasury Stock, at a cost of $30,000, outstanding at June 30, 2010	109,475,600	107,355,700
Accumulated deficit	(105,697,600)	(103,014,700)
Total shareholders' equity	7,758,800	8,885,700
TOTAL LIABILITIES & SHAREHOLDERS' EQUITY	$ 18,278,800	$ 20,496,200

See accompanying notes to the condensed consolidated financial statements

ALANCO TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE MONTHS ENDED MARCH 31, (unaudited)

	2011	2010
NET SALES	$ -	$ -
Cost of goods sold	-	-
GROSS PROFIT	-	-
Corporate expense	262,100	227,100
Amortization of stock-based compensation	-	400
Depreciation and amortizaton	100	200
OPERATING LOSS	(262,200)	(227,700)
OTHER INCOME & (EXPENSES)		
Interest expense, net	(130,400)	(277,400)
Other income (expense), net	-	(800)
LOSS FROM CONTINUING OPERATIONS	(392,600)	(505,900)
INCOME (LOSS) LOSS FROM DISCONTINUED OPERATIONS	800	(514,900)
NET LOSS	(391,800)	(1,020,800)
Preferred stock dividends	(79,400)	(43,600)
NET LOSS ATTRIBUTABLE TO COMMON SHAREHOLDERS	$ (471,200)	$ (1,064,400)
NET LOSS PER COMMON SHARE - BASIC AND DILUTED		
- Continuing operations	$ (0.07)	$ (0.12)
- Discontinued operations	$ 0.00	$ (0.12)
- Preferred stock dividends	$ (0.02)	$ (0.01)
	$ (0.09)	$ (0.25)

- Net loss per share attributable to common shareholders		
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING		
- Basic and diluted	5,528,800	4,331,800

See accompanying notes to the condensed consolidated financial statements

5

ALANCO TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE NINE MONTHS ENDED MARCH 31, (unaudited)

		2011		2010
NET SALES	$	-	$	-
Cost of goods sold		-		-
GROSS PROFIT		-		-
Corporate expense		847,400		657,700
Amortization of stock-based compensation		193,400		99,400
Depreciation and amortizaton		500		600
OPERATING LOSS		(1,041,300)		(757,700)
OTHER INCOME & (EXPENSES)				
Interest expense, net		(384,400)		(657,300)
Other income (expense), net		(9,300)		(2,700)
LOSS FROM CONTINUING OPERATIONS		(1,435,000)		(1,417,700)
LOSS FROM DISCONTINUED OPERATIONS		(1,008,900)		(1,858,800)
NET LOSS		(2,443,900)		(3,276,500)
Preferred stock dividends		(239,000)		(301,800)
NET LOSS ATTRIBUTABLE TO COMMON SHAREHOLDERS	$	(2,682,900)	$	(3,578,300)
NET LOSS PER COMMON SHARE - BASIC AND DILUTED				
- Continuing operations	$	(0.27)	$	(0.34)
- Discontinued operations	$	(0.19)	$	(0.44)
- Preferred stock dividends	$	(0.04)	$	(0.07)
- Net loss per share attributable to common	$	(0.50)	$	(0.85)

shareholders		
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING		
- Basic and diluted	5,352,400	4,215,000

See accompanying notes to the condensed consolidated financial statements

6

ALANCO TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
FOR THE NINE MONTHS ENDED MARCH 31, 2011 (unaudited)

	COMMON STOCK		SERIES D PREFERRED STOCK		SERIES E PREFERRED STOCK		ACCUMULATED	
	SHARES	AMOUNT	SHARES	AMOUNT	SHARES	AMOUNT	DEFICIT	TOTAL
Balances, June 30, 2010	4,665,500	$107,355,700	134,200	$1,333,800	735,000	$3,210,900	$(103,014,700)	$8,885,700
Shares issued for services	3,100	5,300	-	-	-	-	-	5,300
Shares issued for payment on notes and interest	1,100	2,100	-	-	-	-	-	2,100
Shares issued for exercise of warrants	256,200	304,800	-	-	-	-	-	304,800
Value of stock based compensation	-	498,600	-	-	-	-	-	498,600
Private offering, net of expenses	384,300	612,400	-	-	-	-	-	612,400
Series D Preferred dividends, paid as indicated	23,700	37,500	-	-	-	-	-	37,500
Series B Preferred dividends, paid in kind	-	-	-	-	-	-	(85,000)	(85,000)
Series D Preferred dividends, paid or accrued	-	-	-	-	-	-	(31,000)	(31,000)
Series E Preferred dividends, paid or accrued	53,900	83,200	-	-	-	-	(123,000)	(39,800)

Conversion of Pref D to common	129,700	518,900	(51,900)	(518,900)	-	-	-	-
Conversion of Pref E to common	15,000	45,000	-	-	(10,000)	(45,000)	-	-
NASDAQ listing fees and other	-	(17,900)	-	-	-	-	-	(17,900)
Treasury share adjustment	2,000	30,000	-	-	-	-	-	30,000
Net loss	-	-	-	-	-	-	(2,443,900)	(2,443,900)
Balances, March 31, 2011	5,534,500	$109,475,600	82,300	$814,900	725,000	$3,165,900	$(105,697,600)	$7,758,800

See accompanying notes to the condensed consolidated financial statements

ALANCO TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE NINE MONTHS ENDED MARCH 31, (unaudited)

	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	$ (2,443,900)	$ (3,276,500)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	394,600	478,200
Stock-based compensation	498,600	341,800
Stock issued for services	5,300	14,800
Loss on sale of data storage assets	-	48,700
Impairment charge	-	325,000
Interest converted to equity	-	62,500
Fees and interest paid with debt	-	108,100
Changes in operating assets and liabilities:		
Accounts receivable, net	796,100	(758,500)
Inventories, net	(841,700)	370,500
Costs in excess of billings and estimated earnings on uncompleted contracts	12,800	56,600
Prepaid expenses and other current assets	133,300	186,200
Accounts payable and accrued expenses	241,000	(445,100)
Deferred revenue	52,400	(13,700)
Billings and estimated earnings in excess of costs on uncompleted contracts	7,300	(146,900)
Customer advances	(4,500)	677,500
Other assets	42,600	143,600
Net cash used in operations	(1,106,100)	(1,827,200)
CASH FLOWS FROM INVESTING ACTIVITIES		
	(21,500)	(15,200)

Purchase of property, plant and equipment				
Cash received for sale of net data storage assets		-		61,500
Proceeds from sale of net RFID Technology segment assets		2,000,000		-
Net cash provided by investing activities	$	1,978,500	$	46,300

See accompanying notes to the condensed consolidated financial statements

ALANCO TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
FOR THE NINE MONTHS ENDED MARCH 31, (continued)

		2011		2010
CASH FLOWS FROM FINANCING ACTIVITIES				
Proceeds from borrowings	$	784,800	$	812,700
Repayment on borrowings		(2,382,800)		(142,800)
Repayment of capital lease		(13,200)		(11,100)
Proceeds from sale of equity instruments		947,200		965,500
Cash dividends paid		(39,200)		(17,800)
Other		(17,900)		(25,000)
Net cash provided (used) by financing activities		(721,100)		1,581,500
NET INCREASE (DECREASE) IN CASH		151,300		(199,400)
CASH AND CASH EQUIVALENTS, beginning of period		400,500		413,500
CASH AND CASH EQUIVALENTS, end of period	$	551,800	$	214,100
SUPPLEMENTAL SCHEDULE OF CASH FLOW INFORMATION				
Net cash paid during the period for interest	$	376,000	$	323,300
Non-Cash Activities:				
Value of shares issued for services	$	5,300	$	14,800
Value of stock issued for payment of notes	$	2,100	$	748,700
Value of stock issued for payment of interest	$	-	$	67,300
Dividends accrued	$	-	$	29,600
Series B preferred stock dividend, paid in kind	$	85,000	$	77,000
Series D preferred stock dividend, paid in kind	$	-	$	178,500

Series D preferred stock dividend, paid in common	$	37,000	$	105,300
Series D preferred stock converted to line of credit	$	-	$	1,691,100
Series D preferred stock converted to common stock	$	518,900	$	-
Series E preferred stock dividend, paid in common stock or accrued	$	83,700	$	-
Series E preferred stock converted to common stock	$	45,000	$	-
Financing costs paid with debt	$	30,000	$	-
Net data storage assets sold	$	-	$	110,200

See accompanying notes to the condensed consolidated financial statements

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note A – Basis of Presentation and Recent Accounting Pronouncements

Alanco Technologies, Inc., an Arizona corporation ("Alanco" or "Company"), has in recent years reported three business segments: Data Storage, Wireless Asset Management and RFID Technology. At June 30, 2010 and December 31, 2010, in compliance with the Company's plan to divest the Data Storage and RFID Technology segments and invest the proceeds into the Wireless Asset Management segment, the Data Storage and RFID Technology segments had either been sold or were presented as "Assets Held for Sale" and "Liabilities Related to Assets Held for Sale". During the quarter ended March 31, 2011, the Company entered into a definitive agreement to sell the remaining segment, Wireless Asset Management, subject to shareholder approval. The transaction was voted upon at the Company's annual meeting on May 10, 2011. Due to the agreement and approval vote, all operating segments were reported as Discontinued Operations for the quarter ended March 31, 2011. Prior period balances have been reclassified to report all operating segments as discontinued operations for all periods presented.

The Company announced on August 26, 2010 that the Board of Directors had elected to effect a 1 for 8 reverse stock split that was effective on August 27, 2010, when the Company's common stock began trading on a post split-adjusted basis under the interim trading symbol "ALAND" for a period of 20 days, after which the Company's trading symbol returned to "ALAN". (The Company again began trading under the symbol "ALAN" on September 27, 2010.) The Company had previously received authority from its shareholder to effect a reverse split at a ratio within a specified range, if and as determined by the Board of Directors, in order to maintain its NASDAQ listing.

As a result of the reverse split, each eight (8) shares of the Company's Class A Common Stock outstanding at the time of the reverse split was automatically reclassified and changed into one share of common stock, and the total number of common shares outstanding was reduced from approximately 41.7 million shares to approximately 5.2 million shares post split. The reverse stock split resulted in the same adjustment to the Company's outstanding stock options and securities reserved for issuance under its current incentive plans. No fractional shares were issued in connection with the reverse stock split. Upon surrender of their stock certificates, shareholders have received or will receive, cash in lieu of the fractional shares to which they would otherwise be entitled. All per share amounts and outstanding shares, including all common stock equivalents (stock options, warrants and convertible securities) have been restated in the Condensed Consolidated Financial Statements, the Notes to the Condensed Consolidated Financial Statements and the loss per share for all periods presented to reflect the reverse stock split.

The unaudited condensed consolidated financial statements presented herein have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and in accordance with the instructions to Form 10-Q. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. In our opinion, the accompanying condensed consolidated financial statements include all adjustments necessary for a fair presentation of such condensed consolidated financial statements. Such necessary adjustments consist of normal recurring items and the elimination of all significant intercompany balances and transactions.

These interim condensed consolidated financial statements should be read in conjunction with the Company's June 30, 2010 Annual Report filed on Form 10-K. Interim results are not necessarily indicative of results for a full year. Certain reclassifications may have been made to conform prior period financials to the presentation in the current reporting period. The reclassifications had no effect on net loss.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statement and the reported amounts of revenues and expenses during the reporting period. Significant estimates include, but are not limited to, the Company's Wireless Asset Management segment estimates of warranty cost accruals based upon contractual first year warranty obligations.

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

Actual results could differ from these estimates. This segment is being sold with certain sales consideration being escrowed pending a review of changes in working capital. Refer to Note I – Sale of StarTrak.

The Company received a letter of reprimand from Nasdaq on December 28, 2010 concerning Nasdaq's belief that the Company has failed to maintain a majority of independent directors on its Board of Directors in violation of Nasdaq rule 5605 (b)(1), and had a non-independent director on its Nominating Committee in violation of Nasdaq Rule 5605 (e)(1). In particular, Nasdaq has determined that Donald E. Anderson, who served as a director from June 2002 until his resignation on October 4, 2010 and was a member of the Company's Nominating Committee, should not have been classified as an independent director under Nasdaq Rule 5605(a)(2)(d). The Company relied upon outside counsel who determined that the instrument representing the Company's obligation to repay a long term loan by a Trust involving Mr. Anderson constituted a security and that the exception provided by Nasdaq Rule 5605(a)(2)(D)(i) applied. Although there is no Nasdaq Rule or published interpretation to the contrary, Nasdaq staff determined that said obligation of the Company does not constitute a security for purposes of the exemption and Mr. Anderson was therefore not independent.

Nasdaq also found that the Company's violation did not appear to have been the result of a deliberate intent to avoid compliance and was based upon advice of outside counsel. Therefore, the appropriate sanction is issuance of the Letter of Reprimand. The Company was given until its next Annual Meeting of Shareholders scheduled for May 10, 2011 to regain compliance with Nasdaq Rule 5605(b)(1). The annual meeting was held on the date indicated and a slate of five directors, three of which are independent, were elected to serve for a one-year term expiring at the next Annual Meeting of Shareholders or until their successors have been duly elected and qualified. Management believe the Company now complies with Nasdaq Rule 5605(b)(1) and is awaiting a Nasdaq confirmation.

Stock-based compensation - The Company has stock-based compensation plans and reports stock-based compensation expense for all stock-based compensation awards based on the estimated grant date fair value. The value of the compensation cost is amortized at a minimum on a straight-line basis over the requisite service periods of the award (generally the option vesting term).

The Company estimates fair value using the Black-Scholes valuation model. Assumptions used to estimate compensation expense are determined as follows:

- Expected term is determined under the simplified method using an average of the contractual term and vesting period of the award as appropriate statistical data required to properly estimate the expected term was not available;

- Expected volatility of award grants made under the Company's plans is measured using the historical daily changes in the market price of the Company's common stock over the expected term of the award;

- Risk-free interest rate is to approximate the implied yield on zero-coupon U.S. Treasury bonds with a remaining maturity equal to the expected term of the awards; and,

- Forfeitures are based on the history of cancellations of awards granted by the Company and management's analysis of potential future forfeitures.

Long-lived assets and intangible assets – The Company reviews carrying values at least annually or whenever events or circumstances indicate the carrying values may not be recoverable through projected discounted cash flows.

Fair value of financial instruments – The estimated fair values for financial instruments are determined at discrete points in time based on relevant market information. These estimates involve uncertainties and cannot be determined with precision. The carrying amounts of accounts receivable, accounts payable, accrued liabilities, and notes payable approximate fair value given their short-term nature.

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

Recent Accounting Pronouncements

With the exception of those discussed below, there have been no recent accounting pronouncements or changes in accounting pronouncements during the nine months ended March 31, 2011, that are of significance, or potential significance, to us.

In April 2011, the FASB issued guidance which addresses agreements that entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. The guidance is effective for the first interim or annual period on or after December 15, 2011. The Company is currently assessing the impact of this guidance on its financial position and results of operations.

Note B – Stock-Based Compensation and Warrants

The Company has several employee stock option and officer and director stock option plans that have been approved by the shareholders of the Company. The plans require that options be granted at a price not less than market on date of grant and are more fully discussed in our Form 10-K for the year ended June 30, 2010.

The Company uses the Black-Scholes option pricing model to estimate fair value of stock-based awards.

Assumptions for awards of options granted during the nine months ended March 31, 2011 were:

	Awards granted Nine months ended March 31, 2011
Dividend yield	0%
Expected volatility	62%
Weighted-average volatility	62%
Risk-free interest rate	2% - 4%
Expected life of options (in years)	2.0 - 3.75
Weighted average grant-date fair value	$.68

The following table summarizes the Company's stock option activity during the first nine months of fiscal 2011:

	Shares	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Term (1)	Aggregate Fair Value	Aggregate Intrinsic Value (2)

Outstanding July 1, 2010	955,800	$6.27	3.01	$ 4,324,300	-
Shares repriced during period	(866,000)	$5.82	2.78	(3,873,400)	-
Repriced replacement shares	866,000	$1.52	2.78	415,900	-
Granted	172,500	$1.91	4.50	117,600	-
Exercised	-	$0.00	-	-	-
Forfeited or expired	(86,600)	$4.90	-	(391,800)	-
Outstanding March 31, 2011	1,041,700	$1.59	2.66	$ 592,600	$0
Exercisable March 31, 2011	813,400	$1.59	2.34	$ -	$0

(1) Remaining contractual term presented in years.

(2) The aggregate intrinsic value is calculated as the difference between the exercise price of the underlying awards and the closing price of the Company's common stock as of March 31, 2011, for those awards that have an exercise price below the closing price as of March 31, 2011 of $1.14.

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

As of March 31, 2011, the Company had 201,100 warrants outstanding with a weighted average exercise price of $5.77. The life of the outstanding warrants extends from September 30, 2011 through July 9, 2013. The following table summarizes the Company's warrant activity during the first nine months of fiscal 2011:

	Number of Shares	Weighted Average Exercise Price
Warrants Outstanding, June 30, 2010	409,000	$ 11.47
Granted	95,100	2.64
Exercised	(256,200)	1.19
Canceled/Expired	(46,800)	24.00
Warrants Outstanding, March 31, 2011	201,100	$ 5.77

Note C – Assets Held for Sale and Discontinued Operations

The Company implemented a plan during fiscal 2009 to divest the operations of its Data Storage segment and reinvest the proceeds into the remaining business segments. The Company expanded its divestiture plan during the quarter ended September 30, 2009 to include the RFID Technology segment. The Company executed an agreement, during the quarter ended March 31, 2010, to sell substantially all of the assets and liabilities of its Data Storage segment.

On August 18, 2010, the Company announced the divestiture of Alanco/TSI PRISM, Inc. ("TSI") operations, the Company's RFID Technology segment, with the sale of substantially all of the assets and business of TSI to Black Creek Integrated Systems Corp., a private company located in Irondale, Alabama. The transaction, which closed August 17, 2010, consisted of approximately $2 million in cash, and a potential earn-out that could approach five hundred thousand to one million dollars. (The earn-out has not been valued in the transaction due to the lack of supportability.)

At March 31, 2011, the "Assets Held for Sale" and "Liabilities Related to Assets Held for Sale" represent assets retained by seller or receivables resulting from the sales transactions, and liabilities not assumed in the transactions. The divestiture program significantly improved Alanco's financial position by reducing secured debt and eliminating the large operating losses associated with the divested businesses.

In February 2011, the Company entered into a definitive agreement to sell the remaining business segment, Wireless Asset Management, subject to shareholder approval. The transaction was voted upon at the Company's annual shareholders' meeting scheduled for May 10, 2011. Accordingly, at June 30, 2010 and March 31, 2011, all operating segments were reported as "Assets Held for Sale" and "Liabilities Related to Assets Held for Sale". All operating results for those segments were reclassified to discontinued operations for the three and nine months ended March 31, 2011 and 2010. The reclassification of those segment assets and liabilities to "Assets Held for Sale" and "Liabilities Related to Assets Held for Sale" does not affect the reported net loss for the periods presented.

During the fourth quarter ended June 30, 2010, the Company recorded an impairment charge of $4.5 million, reducing the RFID Technology segment values in anticipation of a sale. The impairment charge was made as of June 30, 2010 with knowledge of the RFID Technology transaction sales value as well as knowledge of the segment's operating results for the period from July 1, 2010 through the August 17, 2010 sale date of ($142,200) on sales of $38,700. The operating loss had been accrued at June 30, 2010 as it represented the minimum cost to maintain the operation for sale and resulted in no income or loss from discontinued operations for the RFID Technology segment reported for the nine months ending March 31, 2011. The RFID Technology segment operating loss for the nine months ended March 31, 2010 was $1,153,300, on sales of $674,000.

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

The results for Discontinued Operations (comprised of Wireless Asset Management, Data Storage and RFID Technology business segments) for the nine months and three months ended March 31, 2011 and 2010 were as follows:

	Nine Months Ended March 31, 2011	Nine Months Ended March 31, 2010	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010
Sales				
Wirelesss Asset Management	$ 11,741,200	$ 10,430,000	$ 4,088,400	$ 3,825,800
RFID Technology	38,700	674,000	-	110,300
Data Storage	-	974,100	-	144,600
Total Sales	$ 11,779,900	$ 12,078,100	$ 4,088,400	$ 4,080,700
Gross Profit (Loss)				
Wirelesss Asset Management	$ 4,578,600	$ 4,494,500	$ 1,892,300	$ 1,637,400
RFID Technology	13,500	86,500	-	(27,700)
Data Storage	-	321,000	-	36,700
Total Gross Profit (Loss)	$ 4,592,100	$ 4,902,000	$ 1,892,300	$ 1,646,400
Gross Margin				
Wirelesss Asset Management	39.0 %	43.1 %	46.3 %	42.8 %
RFID Technology	34.9 %	12.8 %	-	-25.1 %
Data Storage	-	33.0 %	-	25.4 %
Total Gross Margin	39.0 %	40.6 %	46.3 %	40.3 %
Selling, General and Administrative Expense				
Wireless Asset Management	$ 5,487,600	$ 4,736,900	$ 1,891,500	$ 1,642,300
RFID Technology	13,500	1,239,800		371,500
Data Storage	99,900	410,400	-	98,800
Data Storage asset impairment charge	-	325,000	-	-
Total SG&A Expense	$ 5,601,000	$ 6,712,100	$ 1,891,500	$ 2,112,600
Income (Loss) from Discontinued Operations				
Wireless Asset Management	$ (909,000)	$ (242,400)	$ 800	$ (4,900)
RFID Technology	-	(1,153,300)	-	(399,200)

Data Storage		(99,900)		(414,400)		-		(62,100)
Loss on Sale - Data Storage		-		(48,700)		-		(48,700)
Total Income (Loss) from Discontinued Operations	$	(1,008,900)	$	(1,858,800)	$	800	$	(514,900)
Capital Expenditures								
Wirelesss Asset Management	$	151,400	$	-	$	16,600	$	-
Data Storage		-		-		-		-
RFID Technology		-		5,600		-		-
Total Capital Expenditures	$	151,400	$	5,600	$	16,600	$	-
Depreciation and Amortization								
Wirelesss Asset Management	$	390,700	$	402,500	$	134,600	$	132,800
Data Storage		3,400		57,100		-		14,800
RFID Technology		-		18,200		-		4,600
Total Depreciation and Amortization	$	394,100	$	477,800	$	134,600	$	152,200

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

Assets and Liabilities related to Discontinued Operations at March 31, 2011 and June 30, 2010 consisted of the following:

	Wireless Asset Management	RFID Technology	Data Storage	Total	
As of March 31, 2011					
Assets held for sale					
Cash	$ 368,200	$ -	$ -	$ 368,200	
Accounts receivable, net	1,690,000	37,300	-	1,727,300	(1)
Inventory, net	2,134,600	2,500	-	2,137,100	(2)
Prepaid expenses and other assets	301,200	-	-	301,200	
Property and equipment, net	316,600	-	-	316,600	
Goodwill	12,575,400	-	-	12,575,400	
Other intangibles	447,200	-	-	447,200	
Total assets held for sale	$ 17,833,200	$ 39,800	$ -	$ 17,873,000	
Liabilties related to assets held for sale					
Billings in excess of costs and estimated earnings	$ -	$ 23,600	$ -	$ 23,600	
Deferred warranty revenue and customer advances	753,500	751,700	-	1,505,200	(3)
Accounts payable and accrued expenses	1,742,600	644,700	-	2,387,300	
Capital leases	9,900	-	-	9,900	
Total liabilities related to assets held for sale	$ 2,506,000	$ 1,420,000	$ -	$ 3,926,000	
As of June 30, 2010					
Assets held for sale					
Cash	$ 248,400	$ -	$ -	$ 248,400	
Accounts receivable, net	2,289,000	135,000	69,900	2,493,900	(1)
Inventory, net	1,222,500	860,900	50,000	2,133,400	(2)
Costs and estimated earnings in excess of billings	-	95,200	-	95,200	

Prepaid expenses and other assets		729,000		328,800		-		1,057,800	
Property, plant and equipment, net		232,900		59,400		-		292,300	
Goodwill		12,575,400		576,700		-		13,152,100	
Other intangibles		770,100		-		-		770,100	
Total assets held for sale	$	18,067,300	$	2,056,000	$	119,900	$	20,243,200	
Liabilties related to assets held for sale									
Billings in excess of costs and estimated earnings	$	-	$	98,700	$	-	$	98,700	
Deferred warranty revenue and customer advances		689,200		768,100		-		1,457,300	(3)
Accounts payable and accrued expenses		1,335,400		631,300		-		1,966,700	
Capital leases		23,200		-		-		23,200	
Total liabilities related to assets held for sale	$	2,047,800	$	1,498,100	$	-	$	3,545,900	

(1) Accounts receivable as of March 31, 2011 and June 30, 2010 are reported net of reserves for the Wireless Asset Management segment of $40,000.

(2) Inventory as of March 31, 2011 is reported net of reserves of $15,000 for the Wireless Asset Management Segment. Inventory as of June 30, 2010 is reported net of reserves for the Wireless Asset Management, RFID Technology and Data Storage segments in the amount of $415,000, $175,000 and $50,000, respectively.

(3) Deferred warranty revenue and customer advances as of March 31, 2011 and June 30, 2010 include $366,100 and $375,400, respectively, of long-term deferred warranty revenue for the Wireless Asset Management segment.

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

Note D - Loss Per Share

Basic and diluted loss per share of common stock was computed by dividing net loss by the weighted average number of shares of common stock outstanding.

Diluted earnings per share are computed based on the weighted average number of shares of common stock and dilutive securities outstanding during the period. Dilutive securities are options, warrants, convertible preferred stock and convertible debt that are freely exercisable into common stock at less than the prevailing market price. Dilutive securities are not included in the weighted average number of shares when inclusion would increase the earnings per share or decrease the loss per share. As of March 31, 2011, there were zero potentially dilutive securities included in the weighted average shares of common stock outstanding as inclusion of outstanding stock options, warrants, and stock issuable upon conversion of debt or preferred stock would be anti-dilutive.

Note E – Equity

During the nine months ended March 31, 2011, the Company issued a total of 869,000 shares, including a 2,000 treasury share adjustment, of Class A Common Stock. Included were 3,100 shares issued for services valued at $5,300, 1,100 shares issued for payment of notes and interest valued at $2,100, 256,200 shares issued for exercise of warrants valued at $304,800, 384,300 shares coupled with 95,100 warrants to purchase Class A Common Stock at $2.64 per share, valued at $612,400, net of $55,400 in expenses issued in a private offering to accredited investors, 23,700 common shares issued in payment of certain Series D Preferred Dividend obligations, valued at $37,500, 53,900 common shares issued in payment of certain Series E Preferred Dividend obligations, valued at $83,200, 129,700 shares, valued at $518,900, issued in the conversion of 51,900 Series D Preferred shares to common shares, and 15,000 shares, valued at $45,000, issued in the conversion of 10,000 Series E Preferred shares to common shares.

The Company declared and paid dividends-in-kind on the Company's Series B Convertible Preferred Stock through the issuance of 8,500 shares of Series B Preferred Stock valued at $85,100. The Company's Preferred Stocks are more fully discussed in the Form 10-K for the year ended June 30, 2010.

On September 16, 2010, the Board of Directors approved the immediate re-pricing of certain outstanding stock options (approximately 866,000 shares to forty-nine individuals) held by current Officers, Directors and employees to $1.52 per share, a 7.9% premium to the closing market price on September 15, 2010 of $1.39. The compensation value created by the re-pricing, as determined under the Black Scholes method, was approximately $298,400 and under current accounting rules results in a non cash expense in current and future periods, not to exceed the vesting periods of the stock options. The Company elected to expense in the quarter ended December 31, 2010, the entire increase in stock based compensation resulting from the re-pricing. Accordingly, the value of employee stock-based compensation recognized for the nine months ended March 31, 2011 amounted to $498,600, including the $298,400 discussed above, compared to $341,800 recognized in the comparable nine months of the prior fiscal year. See Note B – Stock-Based Compensation for additional discussion related to employee stock-based compensation.

During October 2010, the Company raised $304,800 through the exercise of 256,200 warrants. On October 13, 2010, the Company's Board of Directors approved the re-pricing of certain warrants, held by non officers and directors, to purchase 256,200 shares of the Company's Class A Common Stock. The warrants, with exercise prices ranging from $4.00 to $14.40 per share, were re-priced to $1.19 per share, reflecting an approximate 15% discount from the then current market, and required the warrants to be exercised through October 21, 2010. If the warrants were not exercised by the October 21, 2010 date, the exercise price reverted back to the pre-adjusted price. The warrant re-pricing discount represented the Company's estimate of market value, net of costs, of a private placement of an equal amount and was completed to raise required working capital for the Company.

At June 30, 2010, the Company reported 2,000 treasury shares, valued at $30,000, representing the estimated number of Alanco shares to be distributed upon the liquidation of a private Company in which Alanco had ownership.

ALANCO TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

During the quarter ended December 31, 2010, the Company received $18,200 as partial liquidation of its investment. In January 2011, the Company received another $2,800 as a final distribution and accordingly the Company reduced treasury shares at March 31, 2011 to zero, resulting in a loss of approximately $9,000 for the nine month period, reported in the current quarter as other expense.

Note F – Related Party Transactions

The Company has a line of credit agreement (“Agreement”), more fully discussed in the Company’s Form 10-K for the year ended June 30, 2010 with a private trust (“Lender”) controlled by Mr. Donald Anderson, a greater than five percent stockholder of the Company. Mr. Anderson’s investments in the Company are more fully discussed in Note I (below) – Line of Credit and Term Loan and in the Company’s Form 10-K for the fiscal year ended June 30, 2010.

At March 31, 2011 the principal balance due under the Agreement was approximately $4.2 million compared to $5.7 million at June 30, 2010. During the quarter ended September 30, 2010, the Company paid $1.8 million against the credit line from the sale of the net RFID Technology segment assets. During the quarter ended December 31, 2010, the Company borrowed $300,000 under the Agreement. See Note G – Line of Credit and Term Loan for additional discussion of the Agreement.

As discussed in the equity footnote above, during the nine months ended March 31, 2011, the Company issued a total of 23,700 shares of Class A Common Stock, valued at $37,500, in payment of Series D Preferred Stock dividends. 7,900 or 33.3% of the Class A Common Stock issued as Series D Preferred Stock dividend payments went to officers and directors of the Company.

On December 16, 2010, the Company issued a $100,000 note payable to an officer and director for an additional $100,000 of working capital provided to the Company. The note is unsecured, bears interest at a rate of 12% and is payable within thirty (30) days following written demand for such payment by the Holder.

Note G – Line of Credit and Term Loan

On December 16, 2010, the Company and the Anderson Family Trust, a private trust, agreed to an amendment to the Company’s line of credit, entered into in June 2002, which reduced the credit limit on the line to $4.23M from $4.7M, extended the maturity date to January 31, 2011 and decreased the conversion price from $10.00 to $1.37 on the $1 million convertible portion of the debt. The amendment also restricted the $1 million convertible portion to an event of default and placed restrictions on the Company’s issuance of stock. In addition, during the quarter ended March 31, 2011, the Line of Credit maturity date was extended several times to allow the Company time to evaluate available strategic alternatives. The Anderson Family Trust received a $30,000 fee for the amendments, which was added to the loan balance. Currently, the maturity date has been extended to May 16, 2011 as discussed in Footnote J – Subsequent Events.

At March 31, 2011, the Company had reached the maximum outstanding balance under the Line of Credit of $4,230,000. Under the Agreement, the Company must maintain a minimum balance due of at least $2.5 million through its maturity date. Interest is accrued at the prime rate plus 3% (6.25% at March 31, 2011) for any balance up to $2 million and 12% on balances in excess of $2 million.

In addition, ORBCOMM, Inc., an entity that had entered into an agreement to purchase StarTrak Systems, LLC, agreed during the quarter ended March 31, 2011 to loan the Company $300,000, pursuant to a secured promissory note with interest at the rate of six percent per annum. The loan is secured by a second lien on all of the assets of

Alanco and StarTrak. See Footnote I – Sale of StarTrak Systems, LLC for additional discussion of the loan.

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

The Company received a letter of resignation on October 4, 2010, from Don Anderson as a member of the Company's Board of Directors, effective immediately. Mr. Anderson is the owner of approximately 8.6% of the Company's Class A Common Stock and provider of the Company's Line of Credit arrangement discussed above and was the Chairman of the Independent Directors/Nominating Committee, member of the Company's Board of Directors and Trustee of the Anderson Trust. A copy of the resignation, with attachments, submitted with the resignation letter was filed as an Exhibit 99.2 to Form 10-K for fiscal year ended June 30, 2010.

As noted in Footnote F – Related Party Transactions, the Trust advanced $300,000 under the agreement during the month of December 2010. In addition, the maturity date has been extended through May 13, 2011 to allow the Company to evaluate available strategic alternatives. During the quarter ended December 31, 2010, the Company also made the final $100,000 payment on a $4 million term loan financing completed in September 2006 with ComVest Capital LLC.

Note H – Legal

The Company's subsidiary, StarTrak Systems, has recently been made a defendant concerning certain patent infringement claims as follows:

Arrivalstar S.A, et all. v. StarTrak Systems, LLC, et al. Case No.: 4:10-CV-0033. This action was a patent infringement action venued in the United States District Court for the Northern District of Indiana. StarTrak believes that the plaintiff's patents are invalid due to prior art, based, in part, upon the substantial commercial activity concerning the patent claims long before the patents were applied for or issued. However, StarTrak has resolved the action by agreeing to pay $70,000 over a number of monthly payments, thus avoiding substantially greater expenses that would be incurred in defending the action.

Innovative Global Systems LLC v. StarTrak Systems, LLC, et al. Case No.: 6:10-CV-00327. This action is another patent infringement action venued in the United States District Court for the Eastern District of Texas. Again, StarTrak believes that the plaintiff's patents are invalid due to prior art, based, in part, upon the substantial commercial activity concerning the patent claims long before the patents were applied for or issued. Similarly, StarTrak is in discussions with the plaintiff in cooperation with other defendants to resolve the matter by paying a sum substantially less than would be incurred in defending the action. This lawsuit is quite early in the discovery stage and StarTrak's counsel has not formed an opinion concerning the likely outcome. However, the Company's management believes that the suit is without merit and the Company will continue to vigorously defend itself in the matter if it is not soon resolved.

On February 11, 2011, the Company received claims and threatened litigation from Tim Slifkin ("Slifkin") and Tom Robinson ("Robinson"), a director and executive officer, respectively, (both employees of StarTrak) alleging that the Company had not recorded a total of approximately $630,000 of salaries, finder's fees and commissions allegedly earned by Slifkin and Robinson and payable at December 31, 2010. In addition, Slifkin and Robinson claimed that upon the completion of future anticipated transactions they will be owed an additional $335,000 each for a total additional liability of $770,000.

However, in connection with the ORBCOMM acquisition of the StarTrak assets (which was approved by the Company's shareholders at its annual meeting of shareholders held May 10, 2011), the Company entered into a Settlement Agreement and Mutual Release, signed on February 22, 2011 but not effective until signatures were released on February 24, 2011, with Slifkin and Robinson. The agreement provides incentive compensation to Slifkin and Robinson in cash and ORBCOMM stock a total of approximately $85,000 each, upon the successful completion of the sale of StarTrak to ORBCOMM, Inc. In addition, Slifkin and Robinson will receive up to approximately 3.2%, each, of the future potential earn out based upon reported sales for the period March 1, 2011 to February 28, 2012 as discussed in Note I – Sale of StarTrak Systems, LLC, below.

ALANCO TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

StarTrak has recently been served with a Third-Party Complaint by Great American Lines, Inc. and related parties in a lawsuit against them by certain freight shippers in the US District Court for the District of New Jersey, being Case No. 3:10-ev-02023-JAP-TJB. The main case against Great American Lines involves allegations concerning a lost or stolen trailer containing freight owned by the plaintiffs. Great American Lines has brought its Third-Party Complaint against StarTrak alleging that StarTrak breached its contract with Great American Lines to allow Great American Lines to track its trailer and for indemnity. StarTrak has tendered its defense in the lawsuit to its insurance company, but counsel has not yet formed an opinion on the likely outcome. However, the Company's management believes that the suit is without merit and the Company will vigorously defend itself in the matter.

The Company may also, from time to time, be involved in litigation arising from the normal course of business. As of March 31, 2011 there was no other such litigation pending deemed material by the Company.

Note I – Sale of StarTrak Systems, LLC

On February 23, 2011, Alanco Technologies, Inc. Alanco's wholly-owned subsidiary, StarTrak Systems, LLC ("StarTrak") and ORBCOMM Inc. ("ORBCOMM") entered into a Definitive Asset Purchase Agreement (the "Agreement") whereby ORBCOMM will purchase the business and operations of StarTrak Systems, LLC. The transaction is structured as an asset purchase whereby ORBCOMM will acquire substantially all of StarTrak's assets and liabilities. The transaction is considered the sale of substantially all of the assets of Alanco and accordingly required shareholder approval. The proposal was scheduled for a vote at the annual shareholders meeting held on May 10, 2011. (See Item 4. "Submission of Matters to a Vote of Security Holders" below for a summary of the vote results.)